In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 702

THE NEBRASKA SEED COMPANY (TRANSFEROR IN REORGANIZATION WITH UNITED SEEDS, INC.), AND UNITED SEEDS, INC., (TRANSFEREE IN REORGANIZATION WITH THE NEBRASKA SEED COMPANY), PETITIONERS

v.

THE UNITED STATES

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the United States Court of Claims (R. 26–35) is reported in 116 F. Supp. 740.

JURISDICTION

The opinion and judgment of the Court of Claims were entered December 1, 1953. (R. 26.) Motions to alter or amend the judgment or to grant a rehearing or new trial were filed on

December 28, 1953, and were denied on February 2, 1954. (R. 35.) The petition for a writ of certiorari was filed on April 20, 1954. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1255 (1).

QUESTION PRESENTED

The taxpayer acquired all the assets (which included unpaid balances owing on installment sales) from another corporation in a nontaxable exchange. Simultaneously, also in a nontaxable exchange, the taxpayer acquired the assets and assumed the obligations of two other corporations which were the purchasers under the installment contracts. The liabilities assumed by the taxpayer included the unpaid balances on the installment contracts and these liabilities were thus extinguished. Neither the taxpayer nor its predecessor obligee reported any income on the transfer and extinction of the installment obligations. The Court of Claims decided that no gain was recognizable to the transferor corporation on the transfer of the installment obligations but that the deferred profit became taxable to the taxpayer when the obligations were extinguished.

The question is whether the Court of Claims was correct in deciding that, since the taxpayer was liable for but had failed to pay the tax on these profits, it was not entitled to a refund of the tax on the same profits which it had paid as transferee of the transferor corporation.

STATUTES INVOLVED

The applicable portions of the pertinent statutes are set forth in the Appendix, *infra*, pp. 12–14.

STATEMENT

The findings of fact of the Court of Claims may be summarized as follows:

The taxpayer, Nebraska Seed Company, hereinafter referred to as "Nebraska", was a corporation organized under the laws of the State of Nebraska. The taxpayer United Seeds, Inc., hereinafter referred to as "United", is a corporation organized under the laws of the State of Delaware, but with its principal place of business in Ralston, Nebraska. (R. 31–32.)

As of August 1, 1947, United acquired all of the assets and assumed all of the liabilities of Nebraska, pursuant to a plan of reorganization dated July 25, 1947, in exchange for shares of United capital stock. Such reorganization was tax free under the provisions of Section 112 (b) (4) of the Internal Revenue Code. (R. 32.)

As of August 1, 1947, United also acquired under the plan of reorganization all of the assets and assumed all of the liabilities of certain other corporations including the Yankton Realty Company and the Ralston Operating Company. The assets of all these companies were taken in exchange for shares of capital stock of United. The reorganization of these companies was also

a so-called tax free reorganization under Section 112 (b) (4) of the Internal Revenue Code. (R. 32.)

Several years prior to the reorganization, in 1944, Nebraska had sold certain of its assets to the Yankton Realty Company and the Ralston Operating Company, with payment therefor to be made on an installment basis. Nebraska elected to report the profit from such sales on the installment basis as provided by Section 44 (b) of the Internal Revenue Code and did report the profit from such sales consistently and correctly on the installment basis. (R. 32.)

Included in the obligations assumed by United in the plan of reorganization were the installment obligations of Yankton Realty Company and the Ralston Operating Company to Nebraska, and included in the assets received by United were the receivables from these companies which were held by Nebraska. By July 31, 1947, Nebraska had deferred profit on the installment sale which was not reported for federal income tax purposes in the sum of $45,338.39. On the final federal income tax return for Nebraska, the deferred profit was not reported as income. (R. 32–33.)

Under the plan of reorganization of United after the merger of the five corporations, including Nebraska, the Yankton Realty Company and the Ralston Operating Company, all of the assets of Nebraska were transferred to United in ex-

change for shares of stock of the latter corporation on the basis of two shares of $1 par value stock for each $3 value of Nebraska's net worth. In computing the value of the net worth of Nebraska for this purpose, it was permitted to include in its surplus the unrealized profit from the installment obligation due from the Yankton Realty Company and the Ralston Operating Company as the result of the sales of property by Nebraska to those companies in 1944. After this exchange, the stock received from United by Nebraska was distributed to the stockholders of Nebraska, which was then dissolved. (R. 33.)

For the taxable years ending June 30, 1946, and June 30, 1947, Nebraska paid income taxes to the Collector of Internal Revenue at Omaha, Nebraska, in the amounts of $8,360.72 and $17,322.58. For the short taxable period July 1, 1947, to July 31, 1947, Nebraska filed a final federal income tax return showing a net loss of $72,038.33, and using this as a basis filed timely claims for refund for the taxable years ending June 30, 1946, and June 30, 1947, claiming a tentative carry-back of net operating loss of the years ending June 30, 1946, and 1947, in accordance with the provisions of Section 3780 of the Internal Revenue Code. The Collector of Internal Revenue paid tentative tax refunds in the respective sums of $8,360.72 and $14,295.95 for the

taxable years ending June 30, 1946, and June 30, 1947. (R. 33-34.)

Within the period of limitation, the Commissioner of Internal Revenue examined the final federal income tax return of Nebraska and determined that on the final return of that corporation the remaining uncollected deferred profit from installment sales should be reported as income. As a result of the examination a reassessment of a portion of the tentative refunds made under Section 3780 of the Internal Revenue Code resulted and United, as transferee and assignee in reorganization, on or about July 12, 1950, paid the respective sums of $1,416.53 and $14,039.14 in federal income taxes for the taxable years ending June 30, 1946, and June 30, 1947, together with interest in the amounts of $86.70 and $1,336.02 for the respective taxable years. (R. 34.)

On or about October 24, 1950, the taxpayers filed timely claims for refund seeking refunds in the respective sums of $1,416.53 and $14,090.91 for the taxable years ending June 30, 1946, and June 30, 1947, together with interest and/or other amounts properly refundable, using as the basis of their claims the net operating loss carry-backs from the short taxable year from July 1, 1947, to July 31, 1947, to the taxable years ending June 30, 1946, and June 30, 1947. The claims for refund were rejected on July 27, 1951. (R. 34.)

On the basis of the foregoing facts, the Court of Claims concluded that the taxpayers were not entitled to recover and dismissed their petition. Following the judgment of the court, the taxpayers, on December 28, 1953, filed motions to alter or amend judgment or, in the alternative, to grant a rehearing or new trial. The court overruled these motions on February 2, 1954. (R. 35.)

ARGUMENT

1. The decision of the Court of Claims is correct. If, as the court below held, Nebraska did not become taxable with the deferred profits on the installment contracts when they were transferred to United, it is clear that United did become taxable with those profits when, simultaneously, the obligations were extinguished as a result of United's assumption of the obligations of the two corporations which were originally indebted to Nebraska. United, which had successfully urged on the Court of Claims the proposition that Nebraska had incurred no tax liability, does not assert that the profits did not become taxable to it when it became both obligor and obligee and the installment obligations were thereby extinguished. Any such assertion, had it been made, would have been fruitless in view of the provisions contained in the first sentence of Code Section 44 (d) (Appendix, *infra*, pp. 12–13) and its legislative history (H. Rep. No. 2, 70th Cong., 1st Sess., p. 16

(1939–1 Cum. Bull. (Part 2) 384, 394–395)). Nor does United assert that, contrary to the finding of the Court of Claims (R. 31), it had reported this income as its own and had paid the tax.

Under these circumstances, in this refund suit, United was clearly not entitled to a judgment against the United States since it was liable for the tax on the very item of income which gave rise to the refund claim. *Stone* v. *White*, 301 U. S. 532, 535. It would be idle to permit United as transferee to obtain a refund and then adjudge it primarily liable on the same tax. Any refund of tax to which United might be entitled was offset by a tax in the same or substantially the same amount. The ultimate question involved in the claim for refund is whether the taxpayer has overpaid its tax. There has been no showing that United or its predecessor did overpay the tax. In the absence of such a showing, the Government has the right to retain payments already received. *Stearns Co.* v. *United States*, 291 U. S. 54, 62–63; *Lewis* v. *Reynolds*, 284 U. S. 281; *Stone* v. *White*, 301 U. S. 532.

2. There is no merit to the taxpayer's contention that the Court of Claims failed to follow its own Rule 17 with respect to counterclaims. (Br. 14–16.) In general, a counterclaim involves a counter demand containing elements necessary to constitute an independent action for affirmative relief, and not mere defensive matter in denial of

the original claim. *United States* v. *Shaw*, 309 U. S. 495, 503. Rule 17 of the Court of Claims, in accordance with its statutory authority (28 U. S. C., Section 1503), broadens the scope of counterclaims to include claims against a plaintiff not arising out of the transaction or occurrence that is the subject matter of the petition, but neither the statute nor the Rules of the Court of Claims narrows the usual concept of a counterclaim to include a defense to recovery not embracing an independent action for affirmative relief.

Here no counterclaim was pleaded nor can one be inferred to have been demanded. There was only one tax involved, pertaining to the same unreported income, and since Nebraska was dissolved before the action commenced, United was actually the only taxpayer before the court below. Whether the liability for the tax was Nebraska's or United's has become moot in view of the merger leaving United alone as the claimant of the refund, and as the one who owes the tax on the unreported deferred profit. No formal plea of counterclaim was required to prevent the taxpayer from obtaining a refund to which it was not entitled, for at most the matter was in the nature of a setoff. As this Court said in *Stone* v. *White*, 301 U. S. 532, 539: "Here the defense is not a counter demand * * *." See also *Wisconsin Central R'd* v. *United States*, 164 U. S. 190, 212; *Vulcanite Cement Co.* v. *United States*, 74 C. Cls.

692, 717; *United States* v. *Drescher,* 179 F. 2d 863 (C. A. 2d), certiorari denied, 340 U. S. 821.

There is no merit to the taxpayers' contention that United was not before the court below except in a transferee capacity. While United had paid the tax as Nebraska's transferee, United was seeking the refund as its own and, quite plainly, it was not entitled to be enriched in this manner when it was liable for and had not paid the tax on the disputed item of income. Neither can any significance be found in taxpayers' point that separate taxable periods are involved. (Br. 19.) In *United States* v. *Drescher, supra,* where the taxpayer successfully argued that an item of income was not realized in one year, the court, nevertheless, refused to allow the refund in the absence of a showing that the tax had been paid for the other year when it was realized as income. Here, whether recognized to Nebraska or United, the item became income on August 1, 1947.

3. There is no conflict of decisions, and none is alleged in the petition. The taxpayers' attempt to portray this as a case of importance requiring review by this Court ultimately rests on the assumption that the decision below stands for the proposition that a taxpayer has the (Br. 18) "burden of proving himself free of all possible counterclaims in favor of the United States." As we have shown, however, no question of counterclaim is involved and the decision below cannot be interpreted in such a manner.

CONCLUSION

The decision of the court below is correct. This case presents no conflict of decisions, and no question of public interest or importance. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JUNE 1954.

APPENDIX

Internal Revenue Code:

SEC. 44. INSTALLMENT BASIS.

* * * * *

(d) *Gain or Loss upon Disposition of Installment Obligations.*—If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than face value or a sale or exchange—the amount realized, or (2) in case of a distribution, transmission, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. Any gain or loss so resulting shall be considered as resulting from the sale or exchange of the property in respect of which the installment obligation was received. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full. This subsection shall not apply to the transmission at death of installment obligations if there is filed with the Commissioner, at such time as he may by regulation prescribe, a bond in such amount and with such sureties as he may deem necessary, conditioned upon the return as income, by the person receiving any payment on such obligations, of the same proportion of such payment as would be re-

turnable as income by the decedent if he had lived and had received such payment. If an installment obligation is distributed by one corporation to another corporation in the course of a liquidation, and under section 112 (b) (6) no gain or loss with respect to the receipt of such obligation is recognized in the case of the recipient corporation, then no gain or loss with respect to the distribution of such obligation shall be recognized in the case of the distributing corporation.

(26 U. S. C. 1946 ed., Sec. 44.)

SEC. 112. RECOGNITION OF GAIN OR LOSS.

* * * * *

(b) *Exchanges Solely in Kind.*—

* * * * *

(4) *Same.—Gain of corporation.*—No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization.

* * * * *

(6) *Property received by corporation on complete liquidation of another.*—No gain or loss shall be recognized upon the receipt by a corporation of property distributed in complete liquidation of another corporation. For the purposes of this paragraph a distribution shall be considered to be in complete liquidation only if——

(A) the corporation receiving such property was, on the date of the adoption of the plan of liquidation, and has continued to be at all times until the receipt of the

property, the owner of stock (in such other corporation) possessing at least 80 per centum of the total combined voting power of all classes of stock entitled to vote and the owner of at least 80 per centum of the total number of shares of all other classes of stock (except non-voting stock which is limited and preferred as to dividends), and was at no time on or after the date of the adoption of the plan of liquidation and until the receipt of the property the owner of a greater percentage of any class of stock than the percentage of such class owned at the time of the receipt of the property; and

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(26 U. S. C. 1946 ed., Sec. 112.)

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